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Underwood Ranches and Huy Fong
Foods: An Exclusive Relationship

Kelsey Wright*

Baylie Duncan†

Sierra Withrow‡

Bryce Yoshimoto**

*Agribusiness, Cal Poly, San Luis Obispo

†Agribusiness, Cal Poly, San Luis Obispo

‡Agribusiness, Cal Poly, San Luis Obispo

**Agribusiness, Cal Poly, San Luis Obispo

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Kelsey Wright
Baylie Duncan
Sierra Withrow
Bryce Yoshimoto

Underwood Ranches and Huy Fong Foods: An Exclusive Relationship

In the 1980's, Underwood Ranches was struggling financially and in need of a bright new idea to avoid bankruptcy. Third generation owner, Craig Underwood, knew that his family business needed to make some changes, and fast. It was during a fateful call to his seed supplier that Craig was presented with an idea that could save the business. The seed supplier informed Underwood that a small, but rapidly growing, hot sauce company by the name of Huy Fong Foods was in need of a red jalapeno chili supplier for his sauces. Being the businessman that he is, Underwood wrote a letter to the owner of Huy Fong Foods, David Tran, expressing his idea of growing jalapenos for him. This fateful letter led to an exclusive business relationship that has earned much success for the last 26 years. At this time, Tran had been purchasing his jalapenos from the fresh market and other small suppliers, but this just couldn't keep up with the company's growing demand. Underwood's proposal was the perfect solution to Tran's supply issue. Although Tran was excited and eager to acquire more jalapenos, he was skeptical as to whether the small, inexperienced Underwood Ranches could produce the quality and volume of jalapenos that he required.

For the first year, David Tran contracted to buy 50 acres of red jalapeno chili peppers from Underwood Ranches. Once Underwood Ranches had proved their ability to deliver a quality product, the two began contracting more and more acres each year. Four years ago, Huy Fong Foods contracted 17,000 tons from Underwood Ranches. Today, after 26 years in business together, Underwood Ranches produces roughly 58,000 tons of the red jalapenos chilis that are exclusively used by Huy Fong Foods.

RED CHILI PEPPER INDUSTRY BACKGROUND

Red chili peppers, members of the Solanaceae or Nightshade family, are fully mature jalapeno peppers. They stay on the vine longer, giving them time to develop their red color and a slightly sweeter, spicier taste. These peppers have a conical shape, a broad-ended tip, and shiny, smooth skin. The skin of the peppers gain "corking" or wrinkles as they mature.

Named after the city, Jalapa, red jalapeno peppers have been produced in Mexico since the sixteenth century. They were originally sold as a dried or smoked product in Mexican markets. Today, the major Mexican producers cultivate about 40,000 acres a year in the states of Veracruz, Chihuahua, and Oaxaca. In the United States, the main commercial producers of red chili peppers are found in Texas and New Mexico. In the last 30 years, the production of these peppers has been increasing in California as well. This could be a result of increased demand. In the United States from 1995 to 2005, consumption of the red chilies has increased by 38%. From 1993 to 1995, consumption averaged about 4.3 pounds per person every year. By 2005, the average increased to 5.9 pounds consumed per person every year.

UNDERWOOD RANCHES

Their Start

Underwood Ranches is a third-generation company that started in 1867 and is still owned by the Underwood family. They are known for pioneering baby vegetables, spring mix and other specialty vegetables. Underwood Ranches is a family farm located in Ventura County, California which grows a variety of produce for retail and foodservice customers. Their primary crop is jalapenos, which are produced for the famous Sriracha sauce. In addition, they also produce blueberries, varieties of beets, baby carrots, fennel, artichokes, celery root, turnips, rutabagas, parsnips, and other specialty and commodity vegetables. Lima beans, lemon, and the occasional lettuce crop were originally important crops for the company. Each generation, the company has transitioned to and from different crops, depending on what was more profitable. Their crops have transitioned from limas and walnuts, to carrots, pole tomatoes, fordhook limas and broccoli for the Oxnard Frozen Foods, cannery tomatoes for Hunts, and fresh produce for the market. Today, the farm primarily grows red jalapenos for Huy Fong Foods, and farms and ships fresh fruits and vegetables for retail and foodservice customers.

Although Underwood Ranches is a successful and established agribusiness today, they have had to make many strategic business decisions in order to get there. During the depression, the company was having trouble competing with other companies and even came close to bankruptcy. They transitioned between different crops in an effort to boost revenues. However, they didn't catch their break until Craig Underwood's letter saved the company by creating an extremely successful and unique business relationship that has lasted for decades. Today, Underwood Ranches is the sole supplier of red jalapenos for Huy Fong Foods, and Huy Fong Foods is their sole buyer of red jalapenos.

Underwood Ranches Pepper Production

Red jalapenos are an extremely difficult crop to produce, so there are not many farms that currently grow them. It is for this reason that there is very little research or guidelines on how to properly grow these peppers. This lack of information creates a huge barrier to entry for anyone interested in joining the jalapeno growing industry. It took Underwood Ranches many years of creative innovation as well as trial and error to get where they are today. They are currently producing nearly half of all red chili peppers grown in California. Red chili peppers account for about two-thirds of the Underwood Ranches business. Underwood Ranches produces red jalapeno peppers on 44 ranches, which are constantly rotated from chili peppers and cover crops to root crops. Through this system, Underwood Ranches produces about 2,000 acres, equivalent to 58,000 tons, of chili peppers each year.

The largest expenses for Underwood Ranches are seed and transplants. Underwood Ranches obtains their jalapeno seeds from distributors, who provide seeds which have all been hand-pollinated in Vietnam, India, or China. Before Underwood farms begins to produce a specific seed variety, it must first undergo growing trials. These trials take place over a two year period, on three or four of Underwood's ranches, each trial containing 100 plants. The peppers grown from these trials are then evaluated by yield, spice/heat, and adaptability to the location's weather and soil conditions. Through these trials, Underwood Ranches is able to mitigate risk by choosing the correct geography for each specific seed variety. If the trial is successful, a quarter

acre will be planted, which will then increase to five acres and eventually a full crop. During planting, Underwood Ranches plants about four truckloads of transplants per day beginning in mid to late July. The peppers grow best with 90 degree days and 65 degree nights- the weather is most important when the plant is flowering.

During the growing process at Underwood Ranches, little-to-no herbicides are used. This is mainly as a result of the lack of beneficial herbicides available for jalapeno peppers. In addition, management has found that it is cheaper to simply not use them at all. Because red chili peppers are sensitive to root disease, no fumigants are used in the growing process. These peppers are also very water conservative, which helps the company maintain nearly perfect irrigation practices. Excess water is a severe issue in growing the red chili peppers, so Underwood Ranches has implemented drip systems with 95% efficiency. In addition, Underwood Ranches plants 1,000 acres of cover crops per year to keep necessary nutrients in the soil.

Underwood Ranches harvests 35 acres, or an average of 700 tons, of peppers per day. Once the peppers turn their red color, there is a one week window in which all of the peppers must be picked to maintain quality. The harvesting of their jalapeno peppers is an around-the-clock process in early October. Running six days a week, harvesting begins at 4:00am, with the sorting crew beginning shortly after at 5:00am. A night crew is then responsible for sanitizing and Sundays are reserved for any necessary machine repairs. By building their own machines, Underwood Ranches transitioned to a fully mechanical harvest in 2003. This allows for increased efficient harvesting and nearly eliminated the labor required for harvesting. This in turn allows the company maintain low and stable prices, giving them a competitive edge against others. Completely mechanizing has not only helped Underwood Ranches with keeping their pepper prices low, but it has allowed them to reduce their thousand-person workforce to 300 employees.

Underwood Ranches' Innovations within the Pepper Industry

Underwood Ranches has been able to create new innovations within the pepper industry. With only 5000 acres of chili production in California, and Underwood Ranches claiming nearly half, one can imagine that there are not that many other producers. This has led to chili peppers being left behind in regards to new research and innovations, forcing Underwood Ranches' operational manager, Jim Roberts, to create some innovations of their own. The largest and most successful innovation they have created are the machines that they have designed and built for planting and harvesting. Due to a lack of demand, commercialized planting and harvesting equipment for chili peppers is simply unavailable. Luckily, Jim's creative and mechanical background allowed him to make their own by modifying other planters and harvesters. The company's current harvester is made from an old cannery tomato harvester, while their packer is a modified pepper drier. In addition to building their own machines, Underwood Ranches has gone through countless trials and errors over the years to that have enabled them to determine the best practices for producing chilies. They have determined efficient watering practices, how to effectively and economically use cover crops, and overall, how to keep their crops healthy year after year.

With such little research about growing and producing chilies, as well as a lack of machinery available to purchase for chili production, there is a difficult barrier to entry associated with the chili industry. Through years of learning and smart innovations, Underwood Ranches has been able to conquer this barrier and thrive in the world of chilies.

HOT SAUCE INDUSTRY

In recent years, hot sauce has made great strides within its industry. According to IBISWorld, the hot sauce industry has been reported as one of the 10 fastest-growing industries in the United States, with the average company revenue growing by approximately 9.3% percent every year over the last decade. Although the hot sauce industry has had enormous growth, it is still relatively small. This industry employs about 5,500 people throughout 218 hot sauce producing companies. As of now, it is valued at about one billion dollars and is forecasted to continue to grow. Between 2005 and 2010 alone, sales for sauces and marinades went up 20%, and this trend is expected to continue.

With so much growth opportunity, thousands of kitchen and garage cooks, like David Tran, have started experimenting and creating their own concoctions of hot sauces from home. In this way, the hot sauce industry is comparable to the craft brew industry. As Dave Dewitt, producer of the annual National Fiery Foods & Barbecue Show, stated, "It's similar because it's an industry in which people have a vision of a product that they want to create," "So just like microbrewing, people are using innovation as much as they can." Much like the craft brew industry, the hot sauce industry is constantly changing and in high demand.

But what is it that's causing this boom in the hot sauce industry? Researchers believe that it is likely due to a transition in American tastes and preferences. They have noticed a trend in which Americans are transitioning from ketchup to salsas and hot sauces. This is likely because restaurants and grocery stores have been increasing the exposure and popularity of international foods. In addition, an increasing amount of people have been cooking at home in an effort to save money. They are wanting to re-create these international flavors that they have enjoyed while eating out, and hot sauces like Sriracha that make that possible. Another factor that is believed to have had an effect on the hot sauce boom is technology. Originally, it was very difficult just to find bottles for hot sauce. Even David Tran began his hot sauce company by bottling his hot sauce in baby food jars. With today's increased technology, anyone can simply order the jars, labels, and other equipment necessary for starting a hot sauce company. But above all, what is likely the main contributor to the Hot Sauce Industry boom is that Americans have simply fallen in love with the heat of hot sauce!

HUY FONG FOODS

The Beginning of Huy Fong Foods, Inc.

In 1975, David Tran, owner of Huy Fong Foods, began making his popular chili hot sauces in Vietnam. It was here that he created his first hot sauce called Pepper Sa-te. His business started out very small, originally using recycled glass baby food jars as containers and selling his products through friends and family who would then deliver them by bicycle. But it was not long after that in 1979, he escaped communist Vietnam on a freighter named Huey Fong. This became the inspiration for the name of David Tran's beloved company, Huy Fong Foods. As for the rooster emblem that is on each of his products, this was inspired by the Chinese Zodiac sign that he was born under.

After the United States accepted Tran in as a refugee when no other countries would, he settled in California and began making his hot sauces. In 1980, Huy Fong Foods' legacy began in a 5,000 square foot building near Los Angeles' Chinatown. His products included Pepper Sa-te

Sauce, Sambal Oelek, Chili Garlic, Sambal Badjak, and the famous Sriracha Hot Sauce. As a new, small company, Tran would sell whatever he could produce each day and deliver them to Asian restaurants and markets in his blue Chevy van. Some days, he would drive as far as San Diego or San Francisco in order to make these deliveries.

Seven years later, the company was met with great success and outgrew its first facility. Huy Fong Foods purchased a new 68,000 foot facility in Rosemead California. Here, the company thrived as custom machinery, designed by Tran himself, allowed for increases in production capacity to meet the growing demand that they were facing. In order to keep up with this growth, the company purchased another 170,000 square foot building located just down the street. This second facility was used for chili grinding and hot sauce storing. However, Huy Fong Foods continued to grow in sales and needed yet another facility to allow growth. The company purchased a 670,000 square foot building in 2010 as its headquarters, although the state-of-the-art building wasn't operational until a few years later.

This new building has allowed Huy Fong Foods to grow into the iconic company that it is today. David Tran worked tirelessly at it and even designed the multitudes of automated machinery used for hot sauce production. Today, tens of thousands of people visit the headquarters during the chili season for open houses and tours. In addition, his sauces have earned many awards and continue to grow within the hot sauce industry. What started out with humble beginnings has become a hot-sauce giant with Huy Fong Foods bringing in around 6.35 million per year.

Sriracha Business Model

"Everything you expect to read in a textbook about business is exactly opposite", states Jim Roberts, in relation to David Tran's business model for Sriracha and Huy Fong Foods. Everything you may know about how to typically run a business can basically be thrown out the window when analyzing Huy Fong Foods, Inc. In a standard business, there are often multiple investors or loans funding the company. Unlike these businesses, David Tran's empire is almost 100% self-financed. Throughout the years, Tran has been able to pay for all of the company's needs himself, allowing him a lot of freedom to run his business as he wants. Tran has also decided to run his business by using one producer, which allows for purchasing at a set price. Fresh produce purchasing companies like Huy Fong Foods typically have multiple producers and are often constantly negotiating in an effort to receive the best price. Because Underwood Ranches is Huy Fong's sole provider for Jalapenos, the company has a set contract price. This provides David Tran with set low prices, and Underwood Farms with a consistent, profitable sale. This system has allowed Tran to maintain a low price point for Sriracha, which increases sales and demand. This in turn requires Underwood to produce more peppers, increasing his sales as well. As can be seen, this constant price agreement benefits both Huy Fong Foods and Underwood Ranches.

One of the most unique aspects of Huy Fong Foods is that David Tran has never spent any money on advertisement. In comparison to a typical company which may spend thousands of dollars on advertising to increase their sales, Tran's sales continue to increase without any advertisement costs. We wondered how this could be possible, that it just simply did not make any sense. Then Jim Roberts explained other ways Tran can advertise his product without spending money. A few years ago Sriracha was featured on the Cooking Network, and having the red bottle with the rooster sit on the counter while the show went on was a huge success for

Sriracha. It allowed them to get mass exposure quickly. As another way of advertising, Tran does not charge for a license to use his product. If a company wants to use Sriracha in one of their products, Tran allows them to do so free of charge, with the exception to the product that they purchase. He views this free advertisement. For example, veggie sticks approached Tran and wanted to produce a pack of veggie sticks that had Sriracha in it. He agreed and did not charge them the licensing fee, just required them to purchase his product. This was free exposure in Tran's mind, because thousands of bags of veggie sticks hit grocery stores with this company name on it. Tran uses the same approach in regards to companies who want to print the Sriracha label on clothing and hats. Once Tran approves the designs, they printing companies are allowed to use Sriracha's label free of charge. In addition, the company is allowed to keep all profits made from these products while Hoy Fong Farms receives free advertising from people walking around with its brand on their shirts.

Jim Roberts believes that David Tran "Was in the right place at the right time, but he also created a product that captured people's imagination", and that is why Sriracha has been so successful. Although Huy Fong Foods has a truly unique business model unlike any other, more importantly, they have a real and genuine product that people simply love and enjoy.

UNDERWOOD RANCHES AND HUY FONG FOODS TOGETHER

Mutual Relationship

Underwood Ranches and Huy Fong Foods pride themselves in their extremely unique and mutually exclusive business relationship. Underwood Ranches is the sole provider of red chili peppers to Huy Fong Foods, and Huy Fong Foods is Underwood Ranches' sole buyer of jalapeno chili peppers. Jim Roberts of Underwood Ranches described the relationship as a "partnership". David Tran of Huy Fong Foods is extremely involved in what they do at Underwood Ranches. The two businesses have a set price contract that has not changed since 2006. Huy Fong Foods' goal is to keep Sriracha prices low, making the product available to all people. This means that Tran expects to buy his peppers at a low, stable price. Underwood Ranches maintains its low prices because Huy Fong Foods is their largest and most valuable client. Being the largest red pepper producer in California, it is Underwood Ranches' main goal to keep their prices below the producers in Mexico. Keeping each other's best interests in mind, both companies view one another as business partners and friends.

From Red Chili Peppers to Sriracha

After the harvesting process takes place, Underwood Ranches begins the process of pre-sorting the jalapenos and delivering them to Huy Fong Foods with less than half a percent of rejection. Next year, Underwood Farms plans to add pre-washing of the peppers into production. Once sorted, the peppers are then transported in gondolas. A truck full of red chili peppers leaves Underwood Ranches at least every 20 minutes, six days a week, to deliver to Huy Fong's processing plant in Irwindale, CA. The sugars in the red peppers begin to decrease immediately after picking. To ensure Sriracha's intense, sweet flavor, every load of peppers takes less than six hours from the moment they are picked at Underwood Ranches to being ground and ready for processing at Huy Fong's processing plant. The processed Sriracha ingredients are then aged in plastic barrels. Huy Fong bottles their product five days a week year round on nine different packing lines. A single bottle of Sriracha contains about a pound of nine different varieties of Underwood Ranches' peppers.

UNDERWOOD PROBLEMS AND SOLUTIONS

As a company that has been in business for almost 150 years, Underwood Ranches has been faced with a multitude of issues. But whether it be through growing peppers or finding new business opportunities, Underwood Ranches has endured through hardships since 1867. With innovative solutions and a true passion for what they do, Underwood Ranches has proven to be a company capable of overcoming any and all hardships.

Pests have become the one of Underwood Ranches' largest issues within growing peppers. Weevils are Underwood's biggest pest issue. These weevils feed on the jalapeno plants, which can lead to major destruction of the jalapeno or complete loss of the plant. Since jalapenos are a relatively small market, there are not many pesticides that are useful. Underwood implements a good trapping and scouting program in attempts to get ahead of the weevil infestations. Underwood also runs into one of the biggest pest problems in agriculture, which is the growth of weeds and other diseases in the soil. Underwood has tried using Vapam which is a soil fumigant that suppresses or controls the growth of weeds and soil-borne diseases. However, they noticed that using Vapam resulted in loss of all nutrients within the soil, which led to less than desirable results with jalapeno growth. Today, Underwood has turned to the classic method of weed control by planting cover crops. They plant about 1,000 acres of cover crops each year to preserve the nutrients that have been depleted from the jalapenos. This allows for a more efficient and long-term use of the land to keep growing crops without having to relocate and find more suitable soil necessary to grow the jalapenos.

Another production issue that Underwood has faced with growing jalapenos is with the machinery to harvest and plant. When Underwood first started growing jalapenos, there were no machines that suitable for jalapeno growing. Because Jim Roberts had experience in mechanical engineering, he was able to invent the first of the harvesters that Underwood would use. This allowed Underwood Farms to be the only company with the equipment capable of harvesting fresh jalapeno peppers. Underwood recently finished making a planter that will allow them to plant 20 acres a day with a crew of 13 people. This allows Underwood to be more efficient in their planting and harvesting season, as they now have the technology to allow them to have 100% mechanical efficiency.

When it comes to business opportunities Underwood, is always looking for partnerships that will benefit both parties in the long run. However, the problem with looking at the bigger picture is that some customers would rather buy cheaper off the daily market because they are only focused on the daily costs. Jim Roberts said, "Huy Fong is our biggest and best customer". This is due to the relationship that they have forged and the nature of the people there. Underwood recently acquired a contract with In N Out stating that they will become their producer for Cascabella peppers. This contract is just one of the new relationships that Underwood Ranches is looking forward to having in the upcoming years.

Moving Forward

As a company that was able to barely escape bankruptcy, rebuild itself, and prosper into the successful agribusiness that it is today, there is undoubtedly a long and bright future for Underwood Ranches. With sales continuing to grow and a business relationship that is stronger than ever, Underwood Ranch's management is excited for what is to come. The company's

upcoming goals include catching up to the rising demand of Sriracha and continuing to create successful and lasting relationships with companies like Sriracha and In N Out.

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